



OFFICE OF FINANCIAL MANAGEMENT

STATE OF WASHINGTON

Conservation Tax Incentives Water Savings

Report to the Governor and Legislature

This report fulfills the requirements in House Bill 1832, Section 32 (6) from the 2001 legislative session. Specifically, this subsection states:

The Office of Financial Management, in consultation with the departments of Health and Ecology, must evaluate the level of water savings occurring from water suppliers' use of the tax incentive provisions in Section 26 of this act and must report its findings to the Legislature by December 31, 2002.

AUGUST 2002

Evaluation of Water Conservation Tax Incentives

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Conservation Tax Incentives Water Savings

During the 2001 Legislative Session, the Legislature adopted, and the Governor Gary Locke signed into law, a tax-incentive program for water utilities that was created to improve water-use efficiency and promote use of reclaimed water. This legislation established a public utility tax deduction of 75 percent of funds spent to improve consumers' efficient use of water, and a public utility tax exemption applied to 75 percent of receipts for supplying reclaimed water. These tax incentives became effective on May 10, 2001.

The water-use deduction provision of the legislation allows a water utility that takes conservation measures, such as making low-flow showerheads or toilets available to customers, to subtract 75 percent of the cost of those measures from the utility's gross income when it calculates its public utility tax. Last year 550 water utilities paid the tax. For each \$10,000 those utilities spent on eligible conservation measures, the tax incentive provided a savings to the utility of \$377.00.

The water-reclamation exemption provision of the legislation allows a water utility that reclaims sewage or industrial process water and sells it to an entity, such as a golf course or park, to pay a public utility tax on just 25 percent of the receipts of that sale of reclaimed water, rather than 100 percent. There are currently 16 reclaimed water facilities in the state. At this time there is only one that is generating enough revenue to be subject to the public utility tax. That utility has not yet claimed the exemption.

A "Water Rights Trust Account" was also created in the legislation. The Legislature intends to appropriate from the General Fund an amount equaling one-third of the total tax savings resulting from the public utility tax deductions, and place that sum into the new account each fiscal year. Funds in the account will be used to purchase or lease water rights to augment in-stream flows in streams supporting fish stocks that are listed as threatened or endangered under federal law or listed as depressed or threatened by reason of inadequate stream flows under state law.

In addition to the tax incentives, the Legislature mandated that two related reports be prepared. The first report titled **Evaluation of Water Conservation Tax Incentives** (Incentives Report) was submitted to the Legislature in January 2002. The report evaluated the long-term revenue impacts, costs, and benefits of the tax measures, and other potential incentives. It is available in hard copy from the Office of Financial Management (OFM) and on the Internet at www.ofm.wa.gov/water/watertax.htm. This second report evaluates the level of water saved as a result of the tax incentive.

Survey of Water Systems

One of the principal findings of the Incentives Report was that the tax incentive program had not resulted in any significant change in utility behavior to encourage more conservation on the part of their water customers as of the date of the report. Based upon Department of Revenue records, utility participation in the tax incentive program remains low

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with only four additional utilities (an increase from 14 to 18 out of about 500 utilities subject to the tax) claiming the tax deduction since the Incentives Report was prepared. The 18 utilities have claimed a total of about \$822,000 in deductions since the program became effective on May 10, 2001. This has resulted in a savings to the utilities of \$41,000 (with a concurrent loss of state revenue). As mentioned above, no utilities have yet claimed the reclaimed water exemption.

Given the low rate of participation in the tax incentive program, OFM in consultation with the Department of Health (DOH) and the Department of Ecology (Ecology), determined that a phone survey of the participating utilities would be feasible and sufficient to evaluate the level of water saved when used in conjunction with results from an earlier survey of 481 utilities. The earlier survey, conducted in the fall of 2001 under contract to DOH by the Social and Economic Sciences Research Center, Washington State University (WSU), was used in development of the Incentives Report.

DOH staff conducted the phone survey during the latter part of May 2002. A letter of introduction with a list of questions to be asked during the phone interview was sent to each utility approximately two weeks in advance of the phone calls (Appendix 1). The Washington Water Utility Council was consulted on the proposed approach and their comments solicited on a draft of the letter and survey questions. All 18 utilities were very cooperative in completing the survey. Their responses are summarized in Table 1 below.

TABLE 1
Utility Phone Survey Results- May 2002

<u>Utility</u>	<u>New Meas-ures</u>	<u>Water Saved</u>	<u>Anticipate New Measures</u>	<u>Estimate of Savings</u>	<u>Reduce Current Measures</u>	<u>Com-ments</u>
1	NO	NA	NO	NA	NO	NO
2	NO*	YES	NO*	YES	NO	YES
3	NO	NA	NO	NA	H	YES
4	NO	NA	NO	NA	NO	YES
5	NO	NA	NO	NA	NO	YES
6	NO	NA	YES*	NO	NO	YES
7	NO	NA	NO	NA	NO	YES
8	NO	NA	NO	NO	NO	YES
9	NO	NA	NO	NA	NO	YES
10	NO	NA	NO	NA	NO	NO
11	NO	NA	NO	NA	NO	YES
12	NO	NA	NO	NA	NO	NO
13	NO*	NO	NO*	NO	NO	YES
14	NO	NA	NO	NA	NO	YES
15	NO	NA	NO	NA	H	NO
16	NO	NA	NO	NA	NO	YES
17	NO	NA	NO	NA	NO	YES
18	NO	NA	NO	NA	NO	NO

LEGEND:

NO* NO, however savings allowed faster pace of meter installation program already underway.
YES* Would increase conservation effort only if incentive program is extended beyond 2003.
NA Not applicable.
H Deduction helped avert possible conservation program cutback.

Water Saved

None of the 18 utilities that have claimed the deduction indicated they had implemented new conservation measures as a result of the tax incentive. However, two utilities did indicate the savings from the deduction had allowed them to install water service meters at a somewhat faster pace than they would have otherwise been able. These results are consistent with the earlier WSU survey in which only three of the 481 utilities indicated that they probably would spend more on conservation measures as a result of the tax incentive.

Installation of water meters is an essential step in a water conservation program as metering is required to determine current and future water use data that is needed to assess the effectiveness of any conservation efforts. More importantly, the installation of meters in itself typically results in significant water savings as customers recognize they can reduce their water bill by using less water. However, the water savings attributable solely to the faster pace of meter installation is difficult to quantify given that the meter installation programs of the two utilities were underway before the tax incentive program was initiated. Furthermore, the two utilities also indicated that they would continue the installation of meters regardless of the tax incentive.

Based on the DOH phone survey conducted in May 2002 of the 18 utilities that have claimed the tax deduction since it became available, and the WSU survey of 481 utilities conducted in the fall of 2001, it appears that to date the tax incentive has not resulted in any significant increase in new conservation measures being implemented and consequently no significant water savings above that already being achieved by existing conservation measures.

Other Potential Benefits

As shown in Table 1, 13 of the 18 utilities contacted during the phone survey also commented on the tax incentive program. All 13 considered the tax incentive to be a positive factor contributing to their existing conservation efforts. Two of the utilities even considered the incentive to be a factor in convincing their Board of Directors to not cut back their existing conservation efforts and, as discussed above, two others were able to install meters at a faster pace.

Several of the responding utilities commented that the existing tax incentive is probably of more benefit to other utilities than their own for different reasons. However, all expressed support for continuing the program.

Two utilities expressed the opinion that the program would become more effective if it is continued by the Legislature for more than two years. As noted in the Incentives Report, and confirmed by comments received during the phone survey, the budget cycle of some utilities does not lend itself to making immediate changes in conservation programs.

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Changes in utility funding for their conservation programs may not be seen until the tax incentive has been in place for more than two years.

A more complete synopsis of comments provided by the utilities during the phone survey is provided in Appendix 2.

Conclusions

Based on the DOH phone survey conducted in May 2002 of the 18 utilities that have claimed the tax deduction since it became available, and the WSU survey conducted in the fall of 2001 of 481 utilities subject to the tax, it appears that to date the tax incentive has not resulted in any significant increase in water savings above that already being achieved by existing conservation measures.

Although there does not appear to have been any significant water savings to date as a result of the tax incentive, it is important to note that the tax incentive program has been in place for less than a year. As noted in the Incentives Report, the tax incentive may become more effective as additional utilities learn about the program. Also, if the program remains in effect for more than two years, it will allow more utilities to incorporate the savings into their conservation budgets, many of which are on a one- or two- year cycle, and thus have not been able to take into account the tax savings obtained to date.

The conclusions and recommendations in the earlier Incentives Report were supported by the results of the phone survey conducted for this report and readers are referred to the Incentives Report for further information. The report is available in hard copy from OFM and is also available on the web at www.ofm.wa.gov/water/watertax.htm.

May 1, 2002

«contact_title» «PWS_first_name» «PwsContactName»
«SystemName»
«PwsAddress1»
«PwsAddress2»
«PwsCity», «PwsState» «PwsZipCode»

Dear «contact_title» «PwsContactName»:

Last summer the Legislature adopted and Governor Gary Locke signed into law a tax incentive program for water utilities. ESBH 1832 was created to improve water-use efficiency and promote use of reclaimed water. This legislation established a utility tax deduction of 75 percent of funds spent on certain water conservation measures implemented to improve consumers' efficient use of water.

The Department of Health with the Office of Financial Management is required to report the level of water saved as a result of this tax incentive. The Department of Health obtained information from Department of Revenue to verify which water utilities have utilized this tax deduction. Department of Revenue's records indicate your water utility has claimed this deduction recently. Since your utility has claimed this deduction, we are requesting information via a survey from you to complete our report.

We are planning to conduct the survey by phone, rather than asking you to complete the survey and send it back to us. I have attached the survey we will be completing. As you will note, some of the questions regarding water savings may require research, therefore we are sending you the survey in advance. We anticipate making phone calls during the month of May 2002.

Our current records indicate your telephone number is «**PwsContactDayPhone**». If this is incorrect or you would prefer we contact another person in your organization regarding this survey, please provide that information to Bill Thurston at (360) 236-3126 by May 17, 2002.

Thank you for you cooperation in this survey. The results may be instrumental in determining whether or not the current tax deduction is maintained, dropped, or expanded by the Legislature.

Sincerely,

Jim Rioux, Water Resources Lead
Division of Drinking Water

Attachment

Appendix 1

Water Savings Survey Questions

1. To date, has your utility instituted any **new** water conservation measures because of the tax savings resulting from the deduction made available by ESHB 1832?

Yes ☐ Please describe the new conservation measures and when they were put in place.

No ☐ Go to Number 3

2. Have you been able document any water savings attributable to the new measure(s)?

Yes ☐ Please provide the amount of the water saved and a brief description of the type of documentation used. Indicate the time frame over which the savings have occurred. For example, 2 MGD were saved during the months of July and August, 2001 for an annual savings of 62 MG. Source water meters are used to measure the amount of water delivered and amounts were compared to the historic averages for July and August.

No ☐ Have you estimated any water savings that have or will be obtained by instituting the new measures? If you have an estimate, please provide the estimate and the basis for the estimate.

3. Do you anticipate initiating any new water conservation measures in the future as a result of the tax deductions provided in ESHB 1832?

Yes ☐ Please describe the new measures and when you expect to initiate them.

No ☐ Go to Number 5

4. Do you have an estimate of the amount of water you expect to save when you institute the new measures?

Yes ☐ Please provide the estimate of water savings and the basis for the estimate.

No. ☐

5. Would you have reduced or eliminated any of the conservation measures you had in place prior to June 2001 if the tax incentive had not been available?

Yes ☐ Please describe which measures you would have reduced or eliminated.

No ☐

6. Do you have any additional comments or information you would like to provide regarding the tax incentive program or how to improve it?

Synopsis of Utility Comments

As indicated in Table 1, 13 of the 18 utilities contacted for the phone survey provided one or more comments on the tax incentive program. The following summary is intended to capture the general nature and number of the comments rather than specific quotes.

1. We already have a strong conservation program in place and think that all utilities should. The tax savings is welcomed as a positive factor that helps highlight our efforts, and we would like to see it continued. However, it is too small to result in any new conservation efforts. (10 responses)
2. The program would be more effective if those aspects of our conservation efforts focused on region-wide consumers served by our wholesale customers would be considered eligible for the deduction by us or our wholesalers. The current law as interpreted by the Department of Revenue and Department of Health does not allow either us or our wholesalers to claim the deduction. (2 responses) (**Note:** The legislation clearly applies only to final distribution of water to retail customers. Legislation would be needed to include wholesalers of water.)
3. The savings from the deduction will not make it into our conservation budget unless the program is extended since we operate on a two year budget cycle. (2 responses)
4. Initially the deduction was difficult to obtain, as no one in the state was able to explain how to claim it. (2 responses).
5. The amount of savings is small and perhaps there is a better use of state funds. (2 responses)
6. It is a good incentive program for smaller utilities where the savings represent a larger portion of the conservation budget. (2 responses).
7. This may be good for large utilities that can claim a large deduction, but it is not worth it for small utilities (1 response).